



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

Number: **201242015**
Release Date: 10/19/2012

Date: July 27, 2012

Contact Person:

Identification Number:

Contact Number:

Employer Identification Number:

Form Required To Be Filed:

Tax Years:

UIL: 501.00-00; 501.32-00; 501.33-00

Dear :

This is our final determination that you do not qualify for exemption from Federal income tax as an organization described in Internal Revenue Code section 501(c)(3). Recently, we sent you a letter in response to your application that proposed an adverse determination. The letter explained the facts, law and rationale, and gave you 30 days to file a protest. Since we did not receive a protest within the requisite 30 days, the proposed adverse determination is now final.

Because you do not qualify for exemption as an organization described in Code section 501(c)(3), donors may not deduct contributions to you under Code section 170. You must file Federal income tax returns on the form and for the years listed above within 30 days of this letter, unless you request an extension of time to file. File the returns in accordance with their instructions, and do not send them to this office. Failure to file the returns timely may result in a penalty.

We will make this letter and our proposed adverse determination letter available for public inspection under Code section 6110, after deleting certain identifying information. Please read the enclosed Notice 437, *Notice of Intention to Disclose*, and review the two attached letters that show our proposed deletions. If you disagree with our proposed deletions, follow the instructions in Notice 437. If you agree with our deletions, you do not need to take any further action.

If you have any questions about this letter, please contact the person whose name and telephone number are shown in the heading of this letter. If you have any questions about your Federal income tax status and responsibilities, please contact IRS Customer Service at

1-800-829-1040 or the IRS Customer Service number for businesses, 1-800-829-4933. The IRS Customer Service number for people with hearing impairments is 1-800-829-4059.

Sincerely,

Lois G. Lerner
Director, Exempt Organizations

Enclosure
Notice 437
Redacted Proposed Adverse Determination Letter
Redacted Final Adverse Determination Letter



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

Date: June 6, 2012

501.00-00

501.32-00

501.33-00

Contact Person:

Identification Number:

Contact Number:

FAX Number:

Employer Identification Number:

Legend:

LLC =
B =
C =
D =
E =
X =
Letter 1 =
Letter 2 =
Letter 3 =

Dear :

We have considered your application for recognition of exemption from Federal income tax under Internal Revenue Code section 501(a). Based on the information provided, we have concluded that you do not qualify for exemption under Code section 501(c)(3). The basis for our conclusion is set forth below.

FACTS

You are organized as a nonstock corporation under state law. Your articles of incorporation provide that you were formed for the purpose of "mentor[ing] underachieving students with social, emotional, and behavioral problems." Your bylaws provide that you are organized exclusively for charitable and educational purposes and, specifically, "to provide support services to underachieving students, children, and adolescents with social, emotional, and behavioral problems/disorders, and individuals with mental illnesses."

You were formed by LLC. The language you use in your application to describe your goals, objectives, staff, and services is identical to the language used to describe the goals, objectives, staff, and services of LLC on its website, X, a copy of which is enclosed.

In your application you state that your goal is "to provide the support necessary to empower individuals to enhance their overall functioning and define and actively pursue their life goals in a healthy and productive way." You identify three activities – therapeutic mentoring, tutoring, and group therapy – and state that therapeutic mentoring and group therapy are services provided at LLC.

Your initial board of directors comprises six directors, including B, C, D, and E. B and C are business partners in LLC. D is the father of B, and E is the mother of C. According to your application, your directors "are all certified, licensed, degreed, and experienced individuals hired on a part-time/contractual basis." Further, your "multi-disciplinary professional staff includes clinical social workers, psychologists, teachers and counselors who have a wide range of specialized skills and expertise." You share office space with LLC. Accompanying your application was a copy of a form titled "Referral for PRP Services" that appears to be used by LLC. You also said that you will solicit grants from foundations and donations from individuals.

In Letter 1, you said that you will not charge fees for your services. In response to our question whether you refer individuals to LLC or whether LLC refers cases to you, you told us that LLC is a therapeutic community support program. You said that the clients of LLC are required by state law to be actively participating in therapy and have active insurance. If LLC receives a referral, but the referred youth is not actively enrolled in therapy or does not have insurance, you would like to take the case and provide as much service as possible. You said that you are "designed to provide mentoring and support services to at risk youth ... on a volunteer basis." You also said that you would not compensate your board members and that you will not pay rent to LLC for space or equipment.

In Letter 2, in response to our question whether you take into consideration a person's individual or family income in determining whether to provide services to that person, you told us that "individual income level is not a consideration when applying for service. Clients are assessed based on the need for services."

In Letter 3, you told us that it was your intent—

... to seek sponsorship thru the development of positive events and programs that promote a safe and fun environment for kids. From local businesses and networking we will have monthly events/programs that bring awareness to the need for positive mentoring relationships.... We have already secured partnerships with area churches, schools, and businesses to use as event sites. Further, we have created an interest in mentoring services that are greatly needed in the urban community.

You told us that "all funding raised will be used to reimburse mentors for travel and time, and to maintain a certain level of professional services that are tracked and monitored." Finally, you said that you do not plan to lease separate office space.

As part of the Form 1023 application, you are asked to provide financial information in the form of a "statement of revenue and expenses" ("statement"). The statement you provided with your application showed revenue solely from "gifts, grants, and contributions." For each year

reported, you also showed expenses in an amount equal to the amount of revenue reported, though you did not itemize your expenses. In Letter 1, you provided a revised statement. Again, you reported revenue solely from "gifts, grants, and contributions." For each year reported, you again reported expenses equal in amount to the amount of revenue reported. Expenses were categorized as "Occupancy." You told us that "the revenue figure represents the in-kind donations from LLC for office space, supplies, equipment, and utilities." In Letter 2, you provided another statement covering the same years reported in the statement submitted with your application, but this revised statement indicated no revenue or expenses for any of the years reported. In Letter 3, you provided a three year projected budget showing income from "grants, donations, events" and expenses itemized in a variety of categories, the largest amounts being attributable to "mentors/counselors," "community integration/events," and "marketing."

LAW

Section 501(a) of the Code exempts from Federal income taxation organizations described in section 501(c).

Section 501(c)(3) of the Code describes organizations organized and operated exclusively for charitable, religious, educational, or other specified exempt purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Section 1.501(a)-1(c) of the Income Tax Regulations ("regulations") states that the words "private shareholder or individual" in § 501 refer to persons having a personal and private interest in the activities of the organization.

Section 1.501(c)(3)-1(a)(1) of the regulations states that, in order to qualify under § 501(c)(3) of the Code, an organization must be both organized and operated exclusively for one or more exempt purposes. If an organization fails to meet either the organizational or operational test, it is not exempt.

Section 1.501(c)(3)-1(c)(1) of the regulations states that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in § 501(c)(3) of the Code. An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(c)(2) of the regulations provides that an organization is not operated exclusively for one or more exempt purposes if its net earnings inure in whole or in part to the benefit of private shareholders or individuals.

Section 1.501(c)(3)-1(d)(1)(ii) of the regulations provides that an organization is not organized or operated exclusively for one or more purposes specified in § 501(c)(3) unless it serves a public rather than a private interest. Thus, to meet the requirements of § 501(c)(3), it is necessary for an organization to establish that it is not organized and operated for the benefit of private

interests, such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interests.

Section 1.501(c)(3)-1(d)(2) of the regulations provides that the term "charitable" is used in § 501(c)(3) in its generally accepted legal sense. Such term includes relief of the poor and distressed.

P.L.L. Scholarship Fund v. Commissioner, 82 T.C. 196 (1984), held that an organization that raised money for college scholarships from the operation of bingo games on the premises of a lounge was not exempt under § 501(c)(3). Three of the organization's five board members were the two owners and an accountant/director of the lounge. The court stated that more than an insubstantial purpose of the taxpayer's activities was to attract persons, by way of the bingo games, onto the premises of the lounge expecting that they would purchase food and beverages while participating in the games. In fact, the court continued, the taxpayer's activities were, in substantial part, designed to enhance the profitability of the lounge. To ensure this result, the articles of incorporation of the taxpayer named three of its five directors as owners or directors of the lounge, with subsequent directors to be appointed by the board of the lounge. Therefore, the board was and always would be controlled by the directors of the lounge. Consequently, all of petitioner's fundraising activities could be controlled by the owners of the lounge to provide them with maximum benefit. Even though the taxpayer and the lounge kept separate accounts and no cash payments were made from the taxpayer to the lounge for rent or wages, the activities of the two were so interrelated as to be functionally inseparable.

In KJ's Fund Raisers, Inc. v. Comm'r, T.C. Memo 1997-424, the petitioner was organized to raise funds for distribution to charitable causes. Petitioner's business was to sell lottery tickets on the premises of KJ's Place, a lounge owned by Kristine Hurd and James Gould. Hurd and Gould were both officers and directors of petitioner. The Tax Court found that the manner in which petitioner is operated benefits private interests – KJ's Place and its owners. Petitioner's lottery tickets are sold at a single location, KJ's Place, during the regular business hours of KJ's Place, and are overseen by the owners of KJ's Place. The court said that petitioner's practices strongly suggest that Hurd and Gould are free to set policy for their own benefit without objection from petitioner's board, and that KJ's Place had benefitted from the publicity surrounding donations given by petitioner. Although the petitioner was engaged in the exempt activity of raising money for charitable purposes, the court concluded that it was also operated for the substantial private benefit of KJ's Place and its owners. Therefore, petitioner was disqualified from exemption under § 501(c)(3).

Section 4.03 of Rev. Proc. 2012-9, 2012-2 I.R.B. 261, provides that exempt status may be recognized in advance of operations if proposed activities are described in sufficient detail to permit a conclusion that the organization will clearly meet the particular requirements of the section under which exemption is claimed. A mere restatement of purposes or a statement that proposed activities will be in furtherance of such purposes will not satisfy this requirement. The organization must fully describe all of the activities in which it expects to engage, including the standards, criteria, procedures or other means adopted or planned for carrying out the activities, the anticipated sources of receipts, and the nature of contemplated expenditures. Where the organization cannot demonstrate to the satisfaction of the Service that its proposed activities will

be exempt, a record of actual operations may be required before a ruling or determination letter will be issued.

For an organization claiming the benefits of section 501(c)(3), "tax exemptions are matters of legislative grace and taxpayers have the burden of establishing their entitlement to exemptions." Christian Echoes Nat'l Ministry, Inc. v. United States, 470 F.2d 849, 854 (10th Cir. 1972), cert. denied, 414 U.S. 864 (1973). The applicant for tax exempt status under section 501(c)(3) has the burden of showing it "comes squarely within the terms of the law conferring the benefit sought." Nelson v. Comm'r, 30 T.C. 1151, 1154 (1958).

The Tax Court has stated that an application for tax-exempt status "calls for open and candid disclosure of all facts bearing upon [an Applicant's] organization, operations, and finances to assure [that there is not] abuse of the revenue laws. If such disclosure is not made, the logical inference is that the facts, if disclosed, would show that the [Applicant] fails to meet the requirements of section 501(c)(3)." Bubbling Well Church of Universal Love, Inc. v. Comm'r, 74 T.C. 531 (1980). See also, Founding Church of Scientology v. United States, 188 Ct. Cl. 490, 498, 412 F.2d 1197, 1201 (1969), cert. denied, 397 U.S. 1009 (1970). Furthermore, the courts have repeatedly upheld the Service's determination that an organization has failed to establish exemption where the organization fails to provide requested information. "[Applicant] has, for the most part, provided only generalizations in response to repeated requests by [the Service] for more detail on prospective activities....Such generalizations do not satisfy us that [applicant] qualifies for the exemption." Peoples Prize v. Comm'r, T.C. Memo 2004-12 (2004).

ANALYSIS

Failure to Establish Qualification for Exemption

You have asked us to recognize you as an organization described in § 501(c)(3) of the Code. But before we can conclude that you are organized and operated exclusively for one or more exempt purposes described in § 501(c)(3), we must have a clear and unambiguous understanding of your activities. Under the criteria set forth in section 4.03 of Rev. Proc. 2012-9, we will recognize your exempt status only if your operations are described in sufficient detail to permit a conclusion that you will meet the requirements of § 501(c)(3). We find that your application does not meet those criteria. You provide only generalized statements of your goals and objectives. While you outline three activities – therapeutic mentoring, tutoring, and group therapy – you do not provide any explanation of how these activities relate to your goals, nor do you provide a full description of the standards, criteria, procedures, and methods to be used in carrying out such services.

Furthermore, your application is rife with seeming contradictions. For example, in your application you state that your directors are "all certified, licensed, degreed, and experienced," and are "hired on a part-time/contractual basis," but you neither describe the terms of their contracts nor provide copies of written agreements. You also allude to an "interdisciplinary professional staff" of "clinical social workers psychologists, teachers, and counselors." This is the same language used to describe the "staff experience" of LLC's staff on its website, x.

Thus, we are left to infer that your staff is identical to LLC's staff. Your application makes it appear that your directors, or perhaps the staff of LLC (it isn't clear), will be "hired on a part-time/contractual basis" to conduct your activities. But in Letter 1, you say that services will be provided on a volunteer basis by "individuals willing to provide the service," though you do not explain who those individuals might be. Again, in Letter 1, you say that no salaries will be paid to employees, yet, in Letter 3, you list expenses for "mentors/counselors." Your application material included a copy of "PRP referral" form, but the form is addressed to LLC, and you did not list PRP as one of your services. You provided several statements of revenue and expenses, each of which seems to contradict the other. You say that you will solicit grants from foundations and contributions from individuals, but you also tell us that the amounts categorized as gifts, grants, and contributions on your various statements of revenue and expenses represent "in kind donations from LLC of office space, supplies, equipment, and utilities."

Because you have not described your activities clearly and unambiguously, we are unable to conclude that you meet the requirements of § 501(c)(3). Specifically, you have not sufficiently differentiated yourself from LLC to allow us to conclude that you engage primarily in activities that accomplish exempt purposes and are not operated for the benefit of the private interests of the owners of LLC. While, on the one hand, you have not established that your activities further an exempt purpose, it appears, on the other hand, that a more than insubstantial purpose of your activities is to promote the business of LLC.

To be exempt under § 501(c)(3), you must be organized and operated exclusively for charitable purposes. Reg. § 1.501(c)(3)-1(a). You will be regarded as "operated exclusively" for one or more exempt purposes only if you engage primarily in activities which accomplish one or more of the exempt purposes specified in § 501(c)(3). The operational test focuses on the actual purposes an organization advances by means of its activities, rather than on the organization's statement of purpose or the nature of its activities. See American Campaign Academy v. Comm'r, 92 T.C. 1053, 1064 (1989). A single activity might be directed at multiple purposes, both exempt and nonexempt. If the nonexempt purpose is substantial in nature, the organization will not satisfy the operational test. See K.J.'s Fund Raisers, Inc. v. Comm'r, 166 F.3d 1200, (2d Cir. 1998). The burden of proof is on the applicant to demonstrate that it is operated exclusively for exempt purposes and that it does not benefit private interests more than incidentally. See Church of Scientology v. Comm'r, 823, F.2d 1310, 1317 (9th Cir. 1987).

Lack of an Exempt Purpose

Section 501(c)(3) specifies various qualifying exempt purposes, including "charitable" purposes. The term "charitable" is used in its generally accepted legal sense. Section 1.501(c)(3)-1(d)(2). The promotion of health for the benefit of the community is a charitable purpose. See Sound Health Ass'n v. Comm'r, 71 T.C. 158, 177-181 (1978); see also 2 Restatement, Trusts 2d., §§ 368, 372 (1959); 4A Scott & Fratcher, Law of Trusts, §§ 368, 372 (4th ed. 1989). To benefit the community, a charity must serve a sufficiently large and indefinite class. As a corollary to this rule, private interests must not benefit to any substantial degree. See Sound Health Ass'n v. Comm'r at 181. It does not appear that you benefit a large and indefinite charitable class. Rather, it appears that you benefit primarily persons referred to LLC. You told us that you would like to take cases referred to LLC that LLC is unable to serve because the client does not

require active therapy or does not have insurance. Beyond that, it does not appear that you have established any criteria for selecting clients. Since it does not appear that you serve a charitable class of persons, your activities cannot be considered "charitable" within the meaning of § 1.501(c)(3)-1(d)(2) and, therefore, you are not "operated exclusively" for one or more exempt purposes within the meaning of § 1.501(c)(3)-1(c).

Presence of a Substantial Non-Exempt Purpose

When an organization operates for the benefit of private interests such as designated individuals, the creator or his family, shareholders of the corporation, or persons controlled, directly or indirectly, by such private interests, the organization does not operate exclusively for exempt purposes. Prohibited private benefits may include an "advantage, profit, fruit, privilege, gain, or interest." American Campaign Academy v. Comm'r, 92 T.C. 1053, 1065-66 (1989). Should you benefit private interests, you will be deemed to further a nonexempt purpose under § 1.501(c)(3)-1(d)(1)(ii).

You were formed by LLC. Two of your founding directors are business partners in LLC, and another two founding directors are related to the business partners. You share office space with LLC. You use the same referral forms as LLC. The language you use in your application to describe your goals, objectives, staff, and services is identical to the language used to describe the goals, objectives, staff, and services of LLC on its website, x. Since you appear to be so interrelated as to be functionally inseparable from LLC, we can only conclude that your activities could be used to the advantage of LLC. See, e.g., P.L.L. Scholarship Fund v. Comm'r, 82 T.C. at 200.

Although you state that you do not compensate your board members and do not pay rent to LLC, it does appear that your activities provide both monetary and non-monetary benefits to LLC. First, you state that amounts denominated as "gifts, grants, and contributions" on your statement of revenues and expenses "refer to in-kind donations from LLC." We are left with the impression that LLC claims a charitable contribution deduction for the purported value of the office space, supplies, equipment, and utilities it provides to you. Further, you anticipate incurring expenses for "mentors/counselors." Since you do not explain to whom the terms "mentors" and "counselors" refer, but do imply that services are to be provided by the staff of LLC, we are left with the impression that you will funnel any amounts you receive as gifts, grants, and contributions to LLC as payment for services provided by its staff.

Furthermore, we assume that your activities will provide an "advantage, profit, fruit, privilege, gain, or interest" to the owners of LLC in much the same way as the organizations described in P.L.L. Scholarship Fund v. Comm'r and KJ's Fund Raisers v. Comm'r were used to increase the profitability of related for-profit enterprises. As in those cases, your founders are the owners of a for-profit business. As in those cases, your activities are conducted by the staff and on the premises of that for-profit business. And as in those cases, your activities appear designed to increase the profitability of your founder's for-profit business. When we asked you whether you would refer cases to LLC, you did not answer the question we posed, but, instead, stated that you would like to take certain cases referred to LLC. Thus, we infer that cases will be referred between you and LLC. Further, you will seek sponsorships and partnerships with churches,

schools, and businesses to stage community events and programs for the purpose of raising awareness of, and creating interest in, the services you offer. Insofar as such services are the same services offered by LLC, are rendered by the staff of LLC, and are conducted in the offices of LLC, it is inevitable that your efforts to promote these services will benefit LLC and its owners.

Because we are unable to conclude either that you are operated exclusively for an exempt purpose or that you are not operated for the benefit of private interests, we find that you do not qualify as an organization described in § 501(c)(3).

You have the right to file a protest if you believe this determination is incorrect. To protest, you must submit a statement of your views and fully explain your reasoning. You must submit the statement, signed by one of your officers, within 30 days from the date of this letter. We will consider your statement and decide if the information affects our determination.

Your protest statement should be accompanied by the following declaration:

Under penalties of perjury, I declare that I have examined this protest statement, including accompanying documents, and, to the best of my knowledge and belief, the statement contains all the relevant facts, and such facts are true, correct, and complete.

You also have a right to request a conference to discuss your protest. This request should be made when you file your protest statement. An attorney, certified public accountant, or an individual enrolled to practice before the Internal Revenue Service may represent you. If you want representation during the conference procedures, you must file a proper power of attorney, Form 2848, *Power of Attorney and Declaration of Representative*, if you have not already done so. For more information about representation, see Publication 947, *Practice before the IRS and Power of Attorney*. All forms and publications mentioned in this letter can be found at www.irs.gov, Forms and Publications.

If you do not file a protest within 30 days, you will not be able to file a suit for declaratory judgment in court because the Internal Revenue Service (IRS) will consider the failure to protest as a failure to exhaust available administrative remedies. Code section 7428(b)(2) provides, in part, that a declaratory judgment or decree shall not be issued in any proceeding unless the Tax Court, the United States Court of Federal Claims, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted all of the administrative remedies available to it within the IRS.

If you do not intend to protest this determination, you do not need to take any further action. If we do not hear from you within 30 days, we will issue a final adverse determination letter. That letter will provide information about filing tax returns and other matters.

Please send your protest statement, Form 2848 and any supporting documents to this address:

Internal Revenue Service
ATTN:
TE/GE
NCA:
1111 Constitution Ave, N.W.
Washington, DC 20224

You may also fax your statement using the fax number shown in the heading of this letter. If you fax your statement, please call the person identified in the heading of this letter to confirm that he or she received your fax.

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

Lois G. Lerner
Director, Exempt Organizations

Enclosure
Copy of LLC Website